

OFFICE OF TAX APPEALS
STATE OF CALIFORNIA

In the Matter of the Appeal of:)	OTA Case No. 18011203
SMARTMAKE INC.)	Date Issued: December 13, 2018
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OPINION

Representing the Parties:

For Appellant:	Richard Brush, Tax Appeals Assistance Program
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For Respondent:	Eric A. Yadao, Tax Counsel III
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T. STANLEY, Administrative Law Judge: Pursuant to Revenue and Taxation Code section 19324,¹ Smartmake Inc. (appellant) appeals an action by the Franchise Tax Board (FTB or respondent) denying appellant’s claim for refund of \$1,095.67 for taxable year 2013, \$1,101.45 for taxable year 2014, and a \$250 penalty for taxable year 2015.

Appellant waived its right to an oral hearing; therefore, we decide this matter based on the written record.

ISSUES

1. Is appellant entitled to a refund of tax, a late-filing penalty, and interest for taxable year 2013?
2. Is appellant entitled to a refund of tax, a late-filing penalty, an estimated tax penalty, and interest for taxable year 2014?
3. Is appellant entitled to a refund of a \$250 penalty for failure to file a statement of information with the California Secretary of State (SOS) for taxable year 2015?

¹ Unless otherwise indicated, all statutory references (“section” or “§”) are to sections of the Revenue and Taxation Code.

FACTUAL FINDINGS

1. Appellant incorporated in California on July 15, 2013, as Kuhuh Inc. It amended its articles of incorporation on October 4, 2013, and changed its name to Smartmake Inc.
2. Appellant filed statements of information with the SOS on May 3, 2014, and on July 14, 2016. No statement of information was filed in 2015.
3. On August 8, 2016, respondent sent appellant a Corporation Past Due Notice for 2015, requesting that appellant pay a \$250 balance due for a penalty based on its failure to file a 2015 statement of information.² Appellant paid this amount on August 26, 2016.
4. On October 5, 2016, FTB issued a Request for Past Due Corporation Tax Return for taxable year 2013.
5. Appellant filed a 2013 California Corporation Franchise or Income Tax Return (Form 100) on or about February 15, 2017,³ reporting zero income and zero tax liability. A payment of \$1,095.67⁴ was sent to respondent (along with a Smartmake Inc. payment voucher), and was credited to appellant's 2013 account on March 22, 2017. The return was designated a "final return."
6. On or about March 15, 2017, appellant filed a 2014 Form 100, reporting \$0 income and \$0 tax liability. Appellant marked this return a "final return" due to dissolution of the corporation.
7. Appellant sent a letter to respondent on April 15, 2017, claiming it filed a final 2013 tax return and therefore was not required to file 2014 and 2015 tax returns. Additionally, appellant noted that the "state has a policy to waive the 1st year's \$800 minimum tax on the S corporation."⁵ Appellant sent a \$1,101.45 payment to respondent (along with a

² The Corporation Past Due Notice refers to a prior notice to pay the \$250 balance due; however, that document was not submitted to us. Although the notice does not state the reason the penalty was imposed, FTB represented that it was for appellant's failure to file its 2015 statement of information, and appellant has not claimed otherwise.

³ The filed return is dated October 8, 2016; however, respondent's records reflect receiving a letter with the same date without a return. Respondent asserts it received the return on February 15, 2017. The discrepancy does not affect the outcome of this appeal.

⁴ According to respondent, this amount included \$800 of tax, a \$200 late-filing penalty, and \$95.67 of interest.

⁵ Although appellant's correspondence consistently refers to Smartmake Inc. as an "S" corporation, Form 100 was used to file its returns, and no Schedule K-1 forms were issued.

Smartmake Inc. payment voucher), which was credited to appellant's 2014 account on August 9, 2017.⁶

8. Appellant dissolved on May 11, 2017, when it filed a Certificate of Dissolution with the SOS.
9. Appellant claimed refunds for taxes and penalties paid. Respondent denied appellant's claim for 2013 and 2014 by letters dated September 11, 2017. Respondent did not act upon the claim with respect to the penalty assessed for 2015.
10. Appellant timely appealed both denials of its claim for refunds. Additionally, appellant appealed the \$250 penalty for 2015, which OTA accepted as a deemed denial of appellant's refund claim for 2015.

DISCUSSION

Issue 1 - Is appellant entitled to a refund of tax, a late-filing penalty, and interest for taxable year 2013?

As relevant here, every corporation that is incorporated under the laws of the state of California is subject to the minimum franchise tax, from the earlier of the date of its incorporation or commencing to do business within this state, until the effective date of dissolution. (§ 23153(b)(1).) A minimum franchise tax of \$800 is owed annually to the state unless certain exceptions apply. (§ 23153(d).) The exception raised by appellant exempts a corporation that is in its first taxable year after incorporation. (§ 23153(f)(1).)

Appellant incorporated on July 15, 2013, and was in its first taxable year during 2013. It was, therefore, not required to pay the minimum franchise tax, and the penalties associated with failure to pay the minimum tax may not be imposed. Respondent conceded in its opening brief that appellant was not subject to the minimum tax, penalty and interest assessed for 2013, and that upon conclusion of this appeal, it will refund appellant's 2013 payment of \$1,095.67.

Issue 2 - Is appellant entitled to a refund of tax, a late-filing penalty, an estimated tax penalty, and interest for taxable year 2014?

Appellant asserts that it did not have an obligation to file taxes and pay the minimum \$800 franchise tax for 2014 because it never operated the business, and because in 2017, it filed

⁶ According to respondent, this amount included \$800 of tax, a \$200 late-filing penalty, a \$21.95 estimated tax penalty, and \$49.49 of interest.

its 2013 tax return and designated it a “final return.” When a taxpayer designates a return as “final,” respondent must provide the taxpayer with information regarding all documents that are required to be filed with FTB and with the SOS. In an undated letter, FTB fulfilled its obligation to inform appellant that it had received a tax return marked as a “final return.” It gave specific instructions on how to dissolve the corporation, and what steps to take to avoid subsequent liability for the minimum tax.

However, appellant did not file the 2013 “final return” until February 15, 2017, well beyond the 2014 taxable year. Section 23153 clearly applies the minimum tax to appellant since it incorporated in California in 2013 and did not actually dissolve until May 11, 2017, when it filed its Certificate of Dissolution with the SOS. While there are some limited exemptions to the requirement to pay the minimum tax, none of these have been raised for 2014, and none appear to apply to appellant. Appellant is therefore liable for payment of the minimum franchise tax.

For the taxable year at issue, a corporation was required to file its tax return on or before the 15th day of the third month following the close of the tax year. (§ 18601.) Section 19131 requires FTB to impose a late-filing penalty when a taxpayer fails to file a tax return on or before its due date, unless the taxpayer establishes that the late filing was due to reasonable cause and not due to willful neglect. (§ 19131.) The penalty is five percent of the amount of tax required to be shown on the return for every month or fraction thereof that the return is late, up to a maximum of 25 percent. (§ 19131(a).)

To establish reasonable cause, the taxpayer “must show that the failure to file timely returns occurred despite the exercise of ordinary business care and prudence, or that cause existed as would prompt an ordinarily intelligent and prudent businessman to have so acted under similar circumstances.” (*Appeal of Tons*, 79-SBE-027, Jan. 9, 1979.)⁷ Unsupported assertions are not sufficient to satisfy a taxpayer’s burden of proof. (*Appeal of Magidow*, 82-SBE-274, Nov. 17, 1982; *Appeal of Walshe*, 75-SBE-073, Oct. 20, 1975.)

Appellant claims it had reasonable cause for failing to file its 2014 return on time, because 1) it never operated the business after it was incorporated, 2) one or more shareholders moved to China and forgot about the business, and 3) when the business filed its 2013 tax return, it was designated as a “final return.” Appellant further claims that its 2014 tax liability and

⁷ Precedential BOE opinions may be cited as precedential authority to the Office of Tax Appeals unless a panel removes, in whole or in part, the precedential status of the opinion. Precedential BOE opinions are viewable on the board’s website: <<http://www.boe.ca.gov/legal/legalopcont.htm>>.

penalties could have been avoided had respondent notified them of their obligation sooner.

Although it appears that appellant honestly believed no tax was due, the law regarding the obligation to file on time is clear. Moreover, ignorance of the law does not excuse a failure to file a tax return or pay taxes. (*Appeal of Duff*, 2001-SBE-007, Dec. 20, 2001; *Appeal of Oxford Liquor, Inc.*, 79-SBE-052, Mar. 7, 1979.) Appellant did not file its “final return” until February 2017, and then dissolved in May 2017. An ordinarily intelligent and prudent businessperson would have known that a California corporation has an obligation to file tax returns on time and to pay at least the minimum taxes each year. Appellant has not shown reasonable cause for not filing its 2014 return on time.⁸

Appellant also requested a refund for the estimated tax penalty imposed for 2014. A corporation subject to the franchise tax must file a declaration of estimated tax and pay the estimated tax for each year, or part of a year, that it is qualified to do business in this state. (§§ 19023, 19025.) If the amount of estimated tax does not exceed the \$800 minimum franchise tax, the entire amount of the estimated tax shall be due and payable on or before the fifteenth day of the fourth month of the taxable year. (§ 19025(a).) A corporation that underpays its estimated tax is penalized by an addition to tax equal to a specified rate of interest applied to the amount of the underpayment. (§§ 19142, 19144.) That amount generally corresponds to the amount of interest attributable to the underpaid tax. (See § 19521(a)(1)(B)-(C).) There is no general reasonable cause exception to the estimated tax penalty. (*Appeal of Weaver Equipment Co.*, 80-SBE-048, May 21, 1980.)

Here, the evidence is clear that appellant was incorporated in California throughout 2014. The estimated tax penalty is presumed to be correct and “[i]t is well settled . . . that relief from the penalty . . . is not available upon a showing of ‘extenuating circumstances,’ ‘reasonable cause’ or ‘a lack of willful neglect.’ ” (*Appeal of Weaver Equipment Co.*, *supra*.) Appellant does not argue that respondent incorrectly applied the penalty, and it has made no showing that respondent incorrectly calculated the estimated tax penalty. Accordingly, we conclude that appellant is liable for the estimated tax penalty for 2014.

⁸ In its reply brief, appellant claims a refund because the source of the payment was its former shareholder’s personal funds instead of corporate funds. The appellant here is Smartmake Inc., and therefore, the claim for refund made on behalf of the corporation is the only one at issue herein. Appellant included payment vouchers in the name of the corporation, and the payments were credited to the account of the corporation, instead of for the account of any individual.

Issue 3 - Is appellant entitled to a refund of a \$250 penalty for failure to file a statement of information for taxable year 2015?

Corporations Code section 1502 requires every corporation to file an annual statement with the SOS containing certain information. Corporations Code section 2204 provides that after fulfilling certain notice requirements, the SOS shall certify to FTB the name of any corporation which fails to file the required statement. Upon certification, FTB is required to assess a penalty of \$250 against the corporation. (§ 19141; Corp. Code, § 2204(b).) A penalty assessed under section 19141 is a final assessment that is due and payable immediately, subject only to the authority of the SOS to waive the penalty if it determines that the corporation's failure to file the annual statement was "excusable because of reasonable cause or unusual circumstances that justify the failure to file." (Corp. Code, § 2204(f).)

This penalty is assessed by FTB for the SOS. Only the SOS may waive the penalty.⁹ Appellant has cited no authority granting to OTA the authority to waive the penalty, and we are aware of none. Consequently, we conclude that OTA is not authorized to grant relief from the \$250 penalty imposed by respondent pursuant to section 19141.


HOLDINGS

1. Appellant is not liable for tax, penalties, or interest assessed for 2013, and respondent conceded it will refund the entire balance after the conclusion of this appeal.
2. Appellant is liable for the tax, late-filing penalty, estimated payment penalty, and interest assessed for 2014.
3. OTA is not authorized to grant relief from the \$250 penalty imposed by FTB pursuant to section 19141.

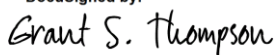
⁹ Instructions for disputing a penalty for failure to file a Statement of Information may be found at: <<https://www.sos.ca.gov/business-programs/business-entities/faqs/#delinquency>>.

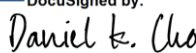
DISPOSITION

FTB's denial of the appellant's claim for refund is reversed for taxable year 2013. We sustain FTB's denial of appellant's refund claim for 2014 and 2015.

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Teresa A. Stanley
Administrative Law Judge

We concur:

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Grant S. Thompson
Administrative Law Judge

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Daniel K. Cho
Administrative Law Judge